SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 395

BRIEF IN SUPPORT OF PETITION

Section 407, Title 40, U. S. C. A.

This Court, in so far as we have been able to find, has not passed on Section 407, Title 40, U. S. C. A.

The text of the statute is:

Assignments by Contractors: Approval: Application of Funds: Penalties

"(a) For the purpose of expediting the actual construction of public works contemplated by section 401-414 of this title and to provide a means of financial assistance to persons under contract with the United States to perform such construction, the President is authorized and empowered, through the Administrator or through such other agencies as he may designate or create, to approve any assignment executed by any such contractor, with the written consent of the surety or sureties upon the penal bond executed in connection with his contract, to any national or State Bank, or his claim against the United States, or any part of such claim, under such contract; and any assignment so approved shall be valid for all purpose, notwithstanding the provisions of section 15 of Title 41 and section 203 of Title 31.

(b) The funds received by a contractor under any advances made in consideration of any such assignment

are hereby declared to be trust funds in the hands of such contractor to be first applied to the payment of claims of subcontractors, architects, engineers, surveyors, laborers, and material men in connection with the project, to the payment of premiums on the penal bond or bonds, and premiums accruing during the construction of such project on insurance policies taken in connection therewith. Any contractor, and any officer, director, or agent or any such contractor, who applies, or consents to the application of, such funds for any other purpose and fails to pay any claim or premium hereinbefore mentioned, shall be deemed guilty of a misdemeanor and shall be punished by a fine of not more than $1,000 or by imprisonment for not more than one year, or by both such fine and imprisonment.

(c) Nothing in this section shall be considered as imposing upon the assignee any obligation to see to the proper application of the funds advanced by the assignee in consideration of such assignment."

This act was passed and became effective June 16, 1933. It is the foundation, bed rock for the entire plan of the economic recovery effected during the Roosevelt Administration.

The functions of the act were transferred to the Federal Works Agency effective July. 1st, 1939.

The Federal Government made available funds for the construction of public works, then for government projects. When the work was first started there was no sure plan of financing the contractors. It was not desired that the government would finance the projects direct. The wisdom of Congress and of the President was called into play to work out a sure and satisfactory plan. The statute under consideration was the result.

A contractor bidding on a job furnished 2 Bonds. One a performance bond that would guarantee that the project would be completed; the other a payment bond guaranteeing

that the completed project would be paid for. This protected the Government as to construction and payment. This act, with the government secures, permitted the contractor, with the written consent of the sureties, to assign the full contract funds to a Bank. The government accepted the assignment and paid the Bank when and as the monies became due by the government on and under the contract.

The assignment passed the title to the Bank. There was no obligation on the contractor to repay; no guarantee that the money would be repaid.

Appeal of Perry, 22 Pa. (10 Harris) 43-60 Am. Dec. 63.
Garretsie vs. *Van Ness,* 2 N. J. Law (1 Penning) 20, 2 Am. Dec. 333.

The contractor, with the written consent of the surety assigned the contract to the Bank, the government approved the assignment. The Bank owed the contractor the contract price less its discount. The government owed the Bank the full contract price. The contractor did not owe the Bank for any part of the funds so advanced. The contractor and his sureties owed the government the completed job.

The court in setting aside the verdict of the jury held that the contractor owed the Bank $1,500,000.00 that had been advanced in payment of the assigned contract. This was an error. The Circuit Court of Appeals affirmed the District Court and committed error.

The Petitioning Creditors Were Secured by Bond—"The Miller Act"

The contracts of the petitioner were covered by the bonds for the performance and payment. The petitioning creditors were not common or unsecured creditors. Glenn was not a creditor. He had paid the Bank by the assignment

of the contracts. The other petitioners' claims were, as material men and subcontractors, secured by the bond; and they were ineligible to join in an involuntary petition in bankruptcy. The court's action in over ruling defendant's motion to dismiss the petition was error.

Who May File a Petition in Involuntary Bankruptcy

The Bankruptcy Acts sets out who may file such a petition. Section 95—Title 11 U. S. C. A.:

Provides that three or more creditors who have provable claims against any person which amount in the aggregate, in excess of the value of securities held by them, if any, to $500.00 or over may file a petition to have him adjudged a Bankrupt.

There were not provable debts shown not fully secured by the performance and payment bonds. The petition should have been dismissed.

Amendments Were Improperly Allowed

The Court allowed the petition to be amended by intervenors, and supplemental petition so as to bring in charges of acts of Bankruptcy alleged to have been committed subsequent to the filing of the original petition. The Circuit Court of Appeals said:

> "Plaintiff's right to any recovery depended upon its right at the inception of the suit, and the nonexistence of the cause of action when the suit was started is a fatal defect which cannot be cured by the accrual of a cause pending suit."
>
> *American Bonding Co.* vs. *Gibson County*, 154 Federal Reporter, 871.

This case had been cited with approval by this Court in the case of U. S. for use of *Portland Cement Company* v.

McCord, 233 U. S. 157, 34 Sup. Ct. 550, Cited in *Eveland* v. *Detroit Machine Tool Co.*, 18 Federal (2nd) 968.

The action of the court in allowing the amendments to bring in alleged acts occurring subsequent to the filing of the petition and the admission of testimony of audits made to show conditions months after the filing of the petition was error.

The defendant's insolvency must be of the date of the acts alleged.

In Re *Ross & O'Brian Iron Works*, 58 Federal (2nd), 961.

In Re *Utrecht Coal Co.*, 63 Federal (2nd), 745.

Starfred Properties vs. *Ettinger*, 131 Federal (2nd) 575.

Jury Verdict Set Aside

The testimony was without dispute that the contractor had assigned to the Memphis Bank contracts of the Government to the value of $10,615,028.12 and that the Bank had advanced only $6,791,789.00 of the purchase price. The balance of the contract price was $3,823,239.02. The $1,500,000.00 that the Bank claimed the contractor owed it was included in the amount paid, shown above. The Du-Main audit showed he had a net worth of over $289,000.00.

The jury found for the defendants. They answered the questions asked by the court favorable to the defendants.

The Court should not have set the verdict aside and entered a judgment of adjudication.

Berry v. *United States*, 312 U. S. 450, 61 S. Ct. 637.

Jacob v. *City of New York*, 315 U. S. 752, 62 S. Ct. 854.

Bailey v. *Central Vermont Railroad Co.*, 319 U. S. 350, 63 S. Ct. 1062.

Blair v. *Baltimore & O. R. Co.*, No. 265, October Term 1944, decided January 19, 1945, and appears in S. Ct. Advance Sheet page 545.

This Court is respectfully petitioned to have record certified up, and to reverse the Circuit Court of Appeals and the District Courts judgment.

Respectfully submitted,

T. J. WILLS,
Counsel for Petitioners.

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